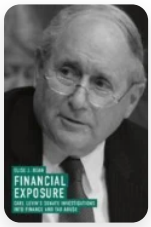
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Stopping Abusive Tax Shelters

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Elise J. Bean

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Abstract

This chapter examines a series of PSI investigations into abusive tax shelters, especially tax shelters used by wealthy individuals and those featuring offshore gimmicks. The first inquiry exposes how accounting firms like KPMG mass-marketed tax shelters in exchange for lucrative fees. The second features a case study of the Wyly brothers who hid hundreds of millions of dollars in a network of 58 offshore corporations and trusts. The third recounts how two billionaires used an offshore tax shelter called the POINT Strategy to dodge capital gains taxes. The chapter shows how the hearings helped spur criminal and civil enforcement actions against the tax shelter promoters, and led to the accounting industry's largely abandoning the U.S. tax shelter business.

> *"Crimes like terrorism or murder or fraud or embezzlement produce instant recognition of the immorality involved. But abusive tax shelters are MEGOs—that means 'my eyes glaze over.' Those who cook up these concoctions count on their complexity to escape scrutiny and public ire."*

Senator Carl Levin, KPMG hearing (Nov. 18, 2003)

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Notes

1. "Senate Panel Seeks Documents on Accountants' Tax Shelters," *Wall Street Journal*, Cassell Bryan-Low (4/22/2003), http://on.wsj.com/2hBblWw. The article did not mention the subpoenas we'd sent to KPMG and Ernst & Young, only document requests, suggesting the leak came from someone with limited knowledge of the PSI investigation.

2. The information in this section is based on the following PSI reports and hearings: "U.S. Tax Shelter Industry: The Role of Accountants, Lawyers, and Financial Professionals; Four KPMG Case Studies: FLIP, OPIS, BLIPS, and SC2," S. Prt. 108-34 (11/18 & 20/2003); "U.S. Tax Shelter Industry: The Role of Accountants, Lawyers, and Financial Professionals," S. Hrg. 108-473, Volumes 1–4 (11/18, 20/2003), https://www.gpo.gov/fdsys/pkg/CHRG-108shrg91043/pdf/CHRG-108shrg91043.pdf (Volume 1); "The Role of Professional Firms in the U.S. Tax Shelter Industry," S. Rept. 109-54 (4/13/2005) (hereinafter "2005 Tax Shelter Committee Report").

3. See, for example, IRS News Release No. IR-2003-84 (7/2/2003) (IRS Settlement with E&Y); "Pricewaterhouse and I.R.S. Settle Tax Shelter Dispute," *New York Times*, David Cay Johnston (6/28/2002), http://nyti.ms/2zUec52.

4. BLIPS is an abbreviation for Bond Linked Issue Premium Structure. OPIS stands for Offshore Portfolio Investment Strategy. FLIP stands for Foreign Leveraged Investment Program. SC2 stands for S-Corporation Charitable Contribution Strategy.

5. 2005 Tax Shelter Committee Report.

6. "KPMG to Pay $456 Million for Criminal Violations in Relation to Largest-Ever Tax Shelter Fraud Case," Department of Justice Press Release (8/29/2005), https://www.justice.gov/archive/opa/pr/2005/August/05_ag_433.html.

7. See "Superseding Indictment of 19 Individuals Filed in KPMG Criminal Tax Fraud Case," Department of Justice Press Release (10/17/2005), http://www.justice.gov/archive/opa/pr/2005/October/05_tax_547.html.

8. *United States v. Stein*, Case No. S1 05 Crim. 0888 (LAK) (District Court SDNY), Opinion (6/26/2006), at 4–6.

9. *United States v. Stein*, 541 F.3d 130 (2nd Cir. 2008).

10. "Manhattan U.S. Attorney Announces Agreement With Ernst & Young LLP To Pay $123 Million To Resolve Federal Tax Shelter Fraud Investigation," Department of Justice Press Release (3/1/2013), http://www.justice.gov/usao-sdny/pr/manhattan-us-attorney-announces-agreement-ernst-young-llp-pay-123-million-resolve.

11. Levin-Coleman Amendment No. 3120 to S. 1637.

12. See Section 818 of H.R. 4520, American Jobs Creation Act of 2004, enacted as Public Law 108-357 (10/22/2004) and codified at 26 U.S.C. 6700.

13. 2005 PCAOB Rule on Auditor Independence and Tax Services, https://pcaobus.org/Rulemaking/Docket017/2004-12-14_Release_2004-015.pdf (proposed rule) and https://pcaobus.org/Rulemaking/Docket017/2005-07-26_Release_2005-014.pdf (final rule); comment letter filed by Senator Levin (2/24/2005), https://pcaobus.org/Rulemaking/Docket017/794_Carl_Levin.pdf.

14. Information about the six case studies is based upon "Tax Haven Abuses: The Enablers, The Tools and Secrecy," S. Hrg. 109-797 (8/1/2006), Volumes 1–4 (hereinafter "Tax Haven Abuses Hearing"), https://www.gpo.gov/fdsys/pkg/CHRG-109shrg29760/pdf/CHRG-109shrg29760.pdf (Volume 1), https://www.gpo.gov/fdsys/pkg/CHRG-109shrg33413/pdf/CHRG-109shrg33413.pdf (Volume 2), https://www.gpo.gov/fdsys/pkg/CHRG-109shrg33414/pdf/CHRG-109shrg33414.pdf (Volume 3), and https://www.gpo.gov/fdsys/pkg/CHRG-109shrg33415/pdf/CHRG-109shrg33415.pdf (Volume 4).

15. A federal court later came to the same factual conclusion. See *SEC v. Wyly*, Case No. 1:10-CV-5760-SAS (District Court SDNY), Opinion and Order (9/25/2014), at 23.

16. For more information on the Wyly ranch, see Tax Haven Abuses Hearing, at 496–502, 508–514.

17. For more information on the Wyly-related jewelry, furnishings, and artwork, see Tax Haven Abuses Hearing, at 518–529.

18. For more information on Security Capital, see Tax Haven Abuses Hearing, at

440–454.

19. See Tax Haven Abuses Hearing, at 161–620.

20. See Hiring Incentives to Restore Employment (HIRE) Act, P.L. 111-147, §533.

21. See *SEC v. Wyly*, Case No. 1:10-CV-5760-SAS (SDNY); "Statement on Jury's Verdict in Case against the Wylys," SEC Press Release, http://www.sec.gov/News/PublicStmt/Detail/PublicStmt/1370541799330. Charles Wyly died in a car accident in 2011, so at the time of trial, the defendants were Sam Wyly and the Charles Wyly estate. See *SEC v. Wyly*, Case No. 1:10-CV-5760-SAS (SDNY), Opinion and Order (1/27/2012) (allowing disgorgement action to proceed against Charles Wyly estate).

22. See, for example, *In Re Sam Wyly*, Case No. 14-35043-BJH (Chap. 11) (NDTX Bankruptcy Court), Memorandum Opinion and Order (8/25/2015), at 7 ("The District Court ultimately concluded that the purpose of the securities fraud was 'to maintain the secrecy of the offshore system and preserve their tax benefits.'").

23. *SEC v. Wyly*, Case No. 1:10-CV-5760-SAS (SDNY), Opinion and Order (9/25/2014).

24. Id., Final Judgment (2/26/2015), http://bit.ly/2zf61n8.

25. See, for example, "Forbes 400," *Forbes* (2006) (ranking Sam Wyly at 354 in the list with an estimated net worth of $1.1 billion), http://bit.ly/292O1KS; and "Forbes 400," *Forbes* (2011) (dropping Sam Wyly from Forbes 400 list after noting his rank of 385 in 2010), http://bit.ly/2itlCor.

26. *In Re Sam Wyly*, Case No. 14-35043-BJH (Chap. 11) (NDTX Bankruptcy

Court), Memorandum Opinion and Order (8/25/2015).

27. Id., Memorandum Opinion (5/10/2016), at 419 (finding tax fraud); unpublished opinion (6/27/2016); "Sam Wyly Tax Bill Totals $1.1B In Fraud Case," *Law360*, Jess Davis (6/27/2016), http://bit.ly/2AaW5Lg.

28. See *United States v. Greenstein, Wilk, and Krane*, Case No. CR08-0296 RSM (USDC WDWA), Superseding Indictment (6/4/2009) (hereinafter "Greenstein Indictment"), at ¶14.

29. The information is based upon the Tax Haven Abuses Hearing, at 230–296.

30. Id., at 237. A later indictment of Jeffrey Greenstein disclosed that he and other Quellos principals were Euram shareholders. See Greenstein Indictment, at ¶8.

31. Id., at 243–244.

32. See Greenstein Indictment.

33. See "Los Angeles Lawyer Sentenced for Tax Evasion and Passport Fraud in Connection with Quellos Tax Shelter Scheme," Department of Justice Press Release (6/10/2011), http://www.justice.gov/archive/usao/waw/press/2011/jun/krane.html.

34. See Greenstein Indictment.

35. See "Former Quellos Executives Plead Guilty in Offshore Tax Shelter Scam Involving More Than $9.6 Billion in Phony Stock Sales," Department of Justice

Press Release (9/13/2010), http://www.justice.gov/archive/usao/waw/press/2010/sep/quellos.html.

36. Tax Haven Abuse Act, S. 681, 110th Congress (2/17/2007).

37. Incorporation Transparency and Law Enforcement Assistance Act, S. 2956, 110th Congress (5/1/2008).

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